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JAMES H. McKENNE

United States Supreme Court

OCTOBER TERM, 1904.

BERTHA DOCTOR AND KATHERINE SAYLES,

Appellants,

against

JOHN J. HARRINGTON, DENNIS A. HARRINGTON, SOL SAYLES COMPANY AND SAYLES, ZAHN COMPANY,

Appellees.

No. 477.

APPELLEES' ARGUMENT.

PHILIP J. BRITT,
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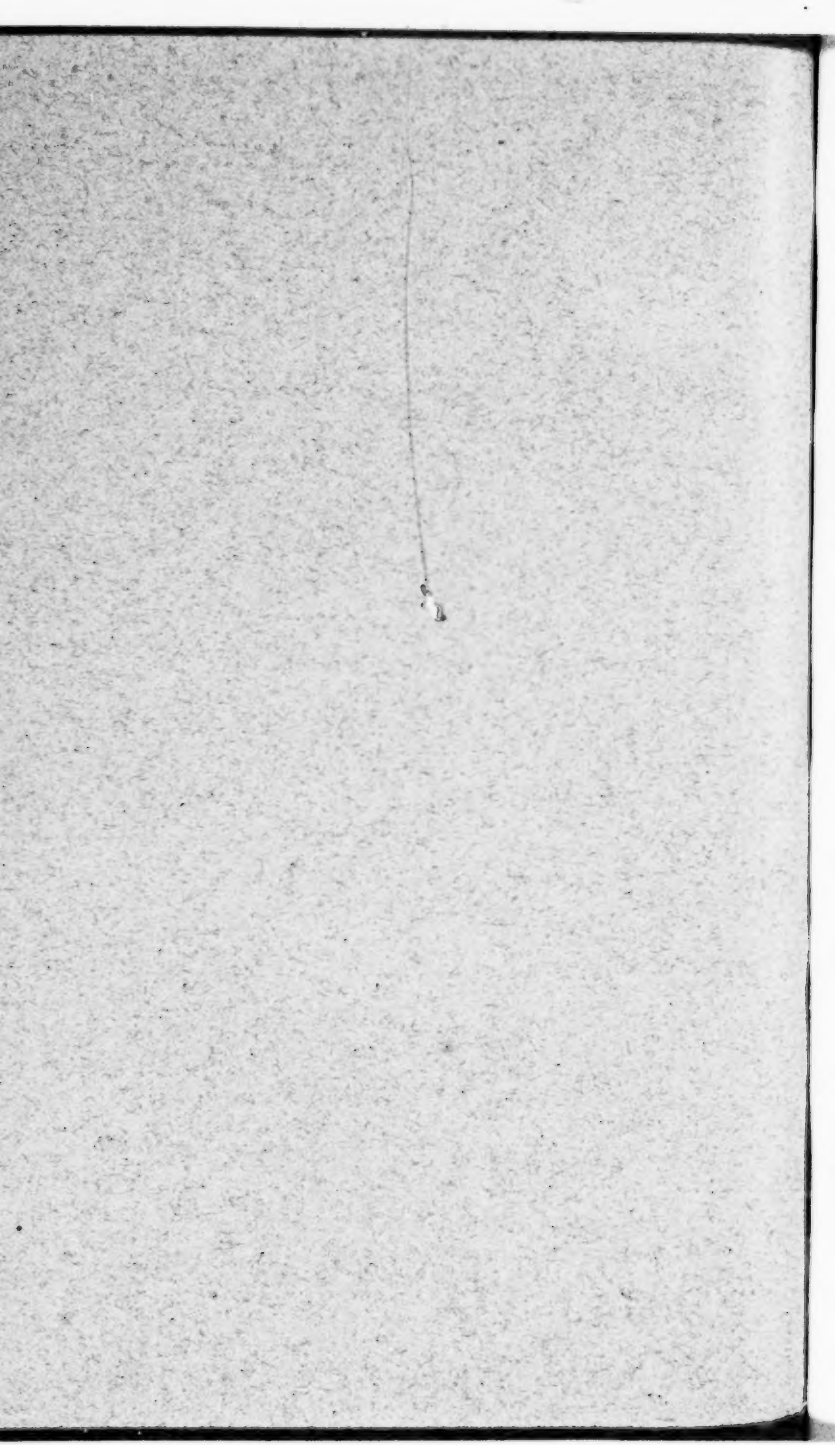
New York.
Stillman Appellate Printing Co.
1905.



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JOHN J. HARRINGTON, DENNIS A. HARRINGTON, SOL SAYLES COMPANY and SAYLES, ZAHN COMPANY,
Appellees.

No. 477

Appeal from the Circuit Court of the United States for the Southern District of New York, Second Circuit.

APPELLEES' ARGUMENT.

The nature of this litigation is stated with substantial accuracy in the appellants' brief. It is conceded that the suit is brought by the complainants, not in their own right, but for the benefit of the defendant Sol Sayles Company, and that they are seeking to maintain this action in the right of that

company. The suit is, therefore, of the nature commonly known as "a derivative action."

The United States Circuit Court for the Southern District of New York dismissed the bill of complaint, for lack of jurisdiction, upon the two grounds which are stated on page 6 of the appellants' brief.

These propositions will now be considered.

ARGUMENT.

I.

This suit cannot be maintained in the Federal Courts, because there is no such diversity of citizenship between the complainants and defendants as is required under the Federal Statutes, since the complainants sue, not in their own right, but as stockholders of the Sol Sayles Company, and are, therefore, to be conclusively presumed, for all the purposes of jurisdiction, to be citizens of the State of New York, under the laws of which State the Sol Sayles Company was organized, and of which State all the other defendants are citizens.

We are brought *in limine* to a consideration of the question, as to what is the nature of this action.

Is it one brought in the right of the complainants, or in the right of the Sol Sayles Company, of which the complainants are stockholders? The bill of complaint indicates, in every line, that the complainants, as such, have absolutely no standing in Court, and that they cannot prevail unless the Sol Sayles Company could as complainant, maintain this action. Had it instituted the suit, the complainants could have no pretence of a cause of action.

Although this proposition stands admitted, as it must be, by the appellants, it will serve to strengthen the appellees' position, by calling attention to the expressions of this and other Courts, in a number of similar cases, which define the nature of such an action.

(a) The action is brought in the right of the corporation.

In *Davenport v. Dows, 18 Wall., 626,* Dows, a citizen of New York, on behalf of himself and all other non-resident citizens of Iowa, who were stockholders in the Chicago, Rock Island and Pacific Railroad Company, filed a bill against the City of Davenport, to stay the collection of a tax alleged to be illegal. The corporation was not made a party defendant, and a demurrer was interposed, which was overruled. On appeal to the United States Supreme Court the decree was reversed, Mr. Justice DAVIS saying:

"That a stockholder may bring a suit when a corporation refuses is settled in Dodge v. Woolsey (18 How., 340), *but such a suit can only be maintained on the ground that the rights of the corporation are involved.* These rights the individual shareholder

is allowed to assert in behalf of himself and associates, because the directors of the corporation decline to take the proper steps to assert them. Manifestly the proceedings for this purpose should be so conducted that any decree which shall be made on the merits shall conclude the corporation. This can only be done by making the corporation a party defendant. *The relief asked is on behalf of the corporation, not the individual shareholder, and if it be granted the complainant derives only an incidental benefit from it. It would be wrong, in case the shareholder were unsuccessful, to allow the corporation to renew the litigation in another suit, involving precisely the same subject matter.* To avoid such a result, a court of equity will not take cognizance of a bill brought to settle a question in which the corporation is the essential party in interest, and as it is made a party to the litigation."

In *Dewing v. Perdicaries, 96 U. S., 197*, Mr. Justice SWAYNE said:

"There are cases in which a corporation, having refused to do its duty, by suing to avert a threatened wrong, a stockholder was permitted to intervene in its stead, making the corporation party. Dodge v. Woolsey, 18 How., 331, is one of this kind. The cases are more numerous where the directors have made themselves personally liable for neglect or breach of duty and the corporation refusing to proceed against them, a stockholder has been permitted to sue in its behalf. *In such cases the corporation is an indispensable party. The refusal must be made definitely to appear; and the avails of the litigation, if there be any, go to the corporation, and are a part of its means as if it had itself sued and recovered.*"

In *Porter v. Sabin, 149 U. S., 473*, the plaintiffs, who were citizens of Illinois and stockholders in the Northwestern Manufacturing and Car Com-

pany, a corporation of Minnesota, brought an action against certain officers of the company, for fraudulent misappropriation of its property, without making the corporation or its receiver a party to the suit. It was held that the action could not be maintained, Mr. Justice GRAY, in explanation of the cause of action, using the following pertinent expression:

"The right to maintain a suit against the officers of a corporation for fraudulent misappropriation of its property is a right of the corporation; and it is only when the corporation will not bring the suit, that it can be bought by one or more stockholders in behalf of all. Hawes v. Oakland, 104 U. S., 450. The suit, when brought by stockholders, is still a suit to enforce a right of the corporation, and to recover a sum of money due to the corporation; and the corporation is a necessary party, in order that it may be bound by the judgment. Davenport v. Dows, 18 Wall., 626."

In *Dickerman v. Northern Trust Company, 176 U. S., 188*, an action in which certain stockholders sought to intervene for the purpose of defending a foreclosure suit in the right of the corporation, Mr. Justice BROWN said:

"It should be borne in mind in connection with the several defences set up by the intervenors that they do not appear here in the capacity of creditors, but as stockholders; *that their rights are the rights of the corporation and must be asserted and enforced through the corporation, and upon the theory that the latter has or threatens, by collusion or otherwise, to neglect the proper defense of the foreclosure suit.* Dodge v. Woolsey, 18 How., 331, 341, 343; Koehler v. Black River Falls Iron Co., 2 Black, 715; Bronson v. LaCrosse &c. Railroad, 2 Wall., 283; Davenport v. Dows., 18 Wall., 626;

Dewing v. Perdicaries, 96 U. S. 193; Hawes v. Oakland, 104 U. S., 450, 460; Greenwood v. Freight Co., 105 U. S., 13; Detroit v. Dean, 106 U. S., 537; Cook on Stockholders, §§645, 659, 750."

The same rules have been fully recognized by the Court of Appeals in New York, in a number of carefully considered cases.

In *Alexander v. Donohoe, 143 N. Y., 203*, that action was by a stockholder to set aside certain transactions and conveyances relating to property belonging to a corporation on the ground that same were fraudulent.

EARL, J., writing for the New York Court of Appeals, said at p. 211:

"Suing as a stockholder the plaintiff's right of action is a derivative one. He sues, not primarily in his own rights, but in right of the corporation. The wrongs of which he complains are wrongs to the corporation. They were not aimed at him and did not involve his personal, individual rights. He suffers as a member of the corporation, and it is the party to sue for and recover damages for the wrongs, or equitable relief against the frauds alleged. The complaint is that all the alleged frauds running through twelve years in the end culminated in final wrong and injury to the corporation, and for relief on account of such wrong and injury a stockholder could only sue in case the corporation upon his demand, or what is equivalent thereto, refused or neglected to sue (Hawes v. Oakland, 104 U. S., 450). And in such an action any defense which a defendant would have if the corporation itself were the actual plaintiff, may be interposed to bar the stockholder."

In *Flynn v. Brooklyn City R. R. Co., 158 N. Y., p. 493*, the plaintiff sued as a stockholder of a street railroad corporation to setaside a lease made by the

corporation and to compel a transfer of the property covered by the lease, and it was decided that the action was representative in character.

VANN, J., said in writing the opinion of the Court at pp. 507, 508:

"Where a majority of the directors, or stockholders, or both, acting in bad faith, carry into effect a scheme which, even if lawful upon its face, is intended to circumvent the minority stockholders and defraud them out of their legal rights, the courts interfere and remedy the wrong. Action on the part of directors or stockholders, pursuant to a fraudulent scheme designed to injure the other stockholders, will sustain an action by the corporation, or, if it refuses to act, by a stockholder, in its stead for the benefit of all the injured stockholders (Leslie v. Lorillard, 110 N. Y., 519-535; Gamble v. Queens County Water Co., 123 N. Y., 91; Sage v. Culver, 147 N. Y., 245; Farmers' Loan & Trust Co. v. N. Y. & N. Ry. Co., 150 N. Y., 410; Hawes v. Oakland, 104 U. S., 450). When a contract founded in fraud is executed by the directors with a third party upon the express approval of a required number of stockholders, with the intention on the part of all concerned to defraud the non-assenting stockholders, and the scheme will naturally result in serious injury to them or to the corporation, a court of equity will set aside the fraudulent transaction and compel the delinquent parties to account. Such is the case before us as we interpret the complaint.

The right of action, however, belongs to the corporation, and should be brought by it as plaintiff, but when it will not bring the suit itself, an aggrieved stockholder, after due demand and a refusal, or unreasonable neglect to proceed, may bring it in his own name upon making the corporation a party defendant (Greaves v. Gauge, 69 N. Y., 154).

It might be well to note here that there are two classes of stockholders actions. In the one class we find those actions in which injury has been done to the stockholder directly, and he sues in his own right for the damages sustained by him; in the other class of cases the injury is done to the corporation, and the stockholder, if he can sue at all, must sue, not in his own behalf, but in behalf of the corporation. The distinction between the two classes of cases is clearly pointed out in *Niles v. N. Y. C. & H. R. R. Co., 176 N. Y., 119.* In that case plaintiff sued for damages resulting from conspiracy to wreck a corporation, and the court sustained a demurrer to the complaint, holding that such an action must be brought by the corporation and not by an individual stockholder.

The Court, per HAIGHT, J., said at pp. 123-124:

"The refusing of traffic and the diversion of funds operated to deplete the company's treasury and was a direct wrong to the corporation. It was an injury for which an action could have been maintained by the corporation, its receiver, if one had been appointed, or by any stockholder, after proper demand, in behalf of the company and for its benefit. In such an action the creditors are vitally interested. They have the right to have the action prosecuted on behalf of the company, so that their interest may be protected and their claims paid out of any recovery which may be obtained.

"True, the plaintiff has suffered a depreciation in the value of his stock as a result of the wrong, and in this respect the injury was personal to the holders of the stock. But every stockholder has suffered from the same wrong, and if the plaintiff can maintain an action for the recovery of the damages sustained by him, every stockholder must be accorded the same right. The injury, however, resulting from the wrong was, as we have seen,

to the corporation. The depreciation in the value of the plaintiff's stock, and that of the other stockholders, was in consequence of the waste and destruction of the property and franchise of the corporation. There are wrongs which if committed against a stockholder entitle him to a right of action against the person committing the wrong for the damages sustained, as, for instance, where a person had been induced to purchase stock in a corporation and pay a higher price than the stock was fairly and reasonably worth, or where the owner of stock had been induced to part with it for a less sum than its true value, by reason of false and fraudulent representations of others with reference to its value (Rothmiller v. Stein, 143 N. Y., 581; Ritchie v. McMullen, 79 Fed. Rep., 522). But these wrongs are distinguishable from those against the corporation. They result in injury to the stockholder upon whom the wrong is practiced, but do not injure the other stockholders of the corporation itself The injuries, however, in this case are not of that character."

And the learned Justice summed up the whole situation in this language, at p. 126:

"We think that the damages belong to the corporation and not to the individual stockholder, and that the judgment should be affirmed with costs."

The rule has been fully recognized in many other cases, including

Smith v. Hurd, 12 Mete., 371.
Allen v. Curtis, 26 Conn., 456.

These authorities establish three propositions: (1) that the complainants in such an action, sue in the right of the corporation; (2) that such action can only be brought by the stockholders where the corporation refuses to sue, and (3)

that where the stockholders sue, the corporation is a necessary party defendant in order that it may be bound by the decree, and that whatever may be recovered shall be administered by it.

(b) *The theory on which the corporation is suable in the Federal Courts.*

The corporation being thus a necessary party, the question arises as to the theory on which the corporation can be brought into a Federal Court. This brings up the long mooted question, as to whether or not a corporation is a citizen within the meanng of the Judiciary Act and its amendments.

Immediately after the passage of the Judiciary Act of September 24, 1789, Chapter 20, Section 11, which conferred jurisdiction on the Circuit Courts of suits of a civil nature in common law and equity "between a citizen of the State where the suit is brought and a citizen of another State," corporations were allowed to sue and be sued in the Circuit Courts only when all the members of the corporation were, and were alleged to be citizens of the state which created the corporation.

Bank of U. S. vs. Dereaux, 5 *Cranch*, 61.
Hope Ins. Co. vs. Boardman, 5 *Cranch*, 57.
Sullivan vs. Fulton Steamboat Co., 6 *Wheat* 540.
Breithaupt vs. Bank of Georgia, 1 *Pet.*, 238.
Commercial Bank vs. Slocomb, 14 *Pet.*, 60.

In 1844, in the case of *Louisville, &c., R. R. Co. vs. Letson (2 How. U. S., 497, 558)*, it was held that it was sufficient to sustain jurisdiction that the corporation was created by a different state from that

of which the opposite party was a citizen, Mr. Justice WAYNE stating that the Court rested its judgment on the ground "that a corporation created by and doing business in a particular state is to be deemed to all intents and purposes as a person, although an artificial person, an inhabitant of the same state, for the purposes of its incorporation, capable of being treated as a citizen of that state, as much as a natural person," and that for these purposes the members of a corporate body must be conclusively presumed to be citizens of the State in which the corporation is domiciled.

This decision was followed in

Marshall vs. Baltimore & Ohio R. R. Co., 16 Ohio, 314, 328.

Covington Drawbridge Co. vs. Shepherd, 20 How., 227, 233.

Ohio & Mississippi R. R. vs. Wheeler, 1 Black, 286, 296.

Muller vs. Dows, 94 U. S., 444.

Steamship Co. vs. Tugman, 106 U. S., 118, 121.

Memphis & Charleston R. R. vs. Alabama, 107 U. S., 581.

Shaw vs. Quincy Mining Co., 145 U. S., 444, 451.

In *St. Louis & San Francisco Railway Co. vs. James* (*161 U. S., 545*) the same doctrine was applied in a case in which the various authorities were carefully reviewed, among others the cases above cited, and as a result of his investigation into the decisions Mr. Justice SHIRAS made the following deductions (p. 562):

"To fully reconcile all the expressions used in these cases would be no easy task, but we think the following propositions may be fairly deduced from them: There is an indisputable legal presumption that a state corporation, when sued or suing in a Circuit Court of the United States, is composed of citizens of the State which created it, and hence such a corporation is itself deemed to come within that provision of the Constitution of the United States which confers jurisdiction upon the Federal Courts in 'controversies between citizens of different states.' * * * The presumption that a corporation is composed of citizens of the State which created it accompanies such corporation when it does business in another State, and it may sue or be sued in the Federal Courts in such other State as a citizen of the State of its original creation.

"We are now asked to extend the doctrine of indisputable citizenship, so that if a corporation of one State, indisputably taken, for the purpose of Federal jurisdiction, to be composed of citizens of such State, is authorized by the law of another State to do business therein, and to be endowed, for local purposes, with all the powers and privileges of a domestic corporation, such adopted corporation shall be deemed to be composed of citizens of the second State, in such a sense as to confer jurisdiction on the Federal Courts at the suit of a citizen of the State of its original creation.

"We are unwilling to sanction such an extension of a doctrine which, as heretofore established, went to the very verge of judicial power. That doctrine began, as we have seen, in the assumption that State corporations were composed of citizens of the State which created them; but such assumption was one of fact, and was the subject of allegation and traverse, and thus the jurisdiction of the Federal Courts might be defeated. *Then, after a long contest in this court, it was settled that the presumption of citizenship is one of law, not to be defeated by allegation or evidence to the contrary.* There we are content to leave it."

In *Barrow Steamship Co. vs. Kane (170 U. S., 100)* Mr. Justice GRAY, after citing the early cases on the subject of jurisdiction over corporations, said:

"But the earlier cases were afterwards overruled; and it has become the settled law of this court that, for the purposes of suing and being sued in the courts of the United States, a corporation created by and doing business in a State is, although an artificial person, to be considered as a citizen of the State as much as a natural person; *and there is a conclusive presumption of law that the persons composing the corporation are citizens of the same State with the corporation.*"

In *Southern Railway Co. vs. Allison (190 U. S., 326)* it was held that, although a statute of North Carolina provided that a foreign railroad company desiring to own property or carry on business, or exercise any corporate franchise within the State, must comply with certain specified provisions of the statute, and on complying therewith shall become a domestic corporation, such fact does not affect the character of the original corporation, and it does not thereby become a citizen of North Carolina so far as to affect the jurisdiction of the Federal Courts upon a question of diverse citizenship. In the course of his opinion, Mr. Justice PECKHAM said:

"It early became material to inquire into the nature of the status of corporations with regard to the jurisdiction of Federal Courts under the Constitution and laws of the United States. A recent statement of the law on that subject is contained in the case of St. Louis and San Francisco Railway Co. v. James (161 U. S., 545). It was said by

Mr. Justice SHIRAS in delivering the opinion of the Court in that case, that after considerable contention in the Courts it was finally determined by this Court that the citizenship of a corporation was that of the State originally creating it, and that it was a presumption of law that the members of the corporation were citizens of the same State."

See, also,

Great Southern Fire Proof Hotel Co. vs. Jones, 177 U. S., 456.

Taylor vs. Illinois Central Ry. Co., 89 Fed. Rep., 119.

These authorities have been approved in the recent case of *Thomas v. Board of Trustees, 195 U. S., 207,* where Mr. Justice HARLAN, after a full review of the decisions above cited, and speaking for a unanimous Court, says:

"That the jurisdiction of a Circuit Court of the United States is limited in the sense that it has no jurisdiction except that conferred by the Constitution and laws of the United States; that a cause is presumed to be without its jurisdiction unless the contrary affirmatively appears; that such jurisdiction, or the facts upon which in legal intendment it rests, must be distinctly and positively averred in the pleadings or should appear affirmatively and with equal distinctness in other parts of the record, it not being sufficient that jurisdiction may be inferred argumentatively; *and that, for the purpose of suing and being sued in a Circuit Court of the United States, the members of a local 'corporation' are conclusively presumed to be citizens of the State by whose laws it was created,* and in which alone the corporate body has a legal existence; are propositions so firmly established that further discussion of them would be both useless and inappropriate."

We have thus repeated declarations by this Court that jurisdiction in the Federal Courts over a corporation depends upon its status, which in turn is dependent upon the State of its original incorporation, and upon the conclusive, irrebuttable presumption of law that all of the members of the corporation, that is, all of its stockholders, are citizens of the State in which the corporation was organized.

Here, therefore, the Sol Sayles Company is to be treated as a citizen of New York, because it was there incorporated and because it is presumed as matter of law, irrespective of what the actual facts may be, that all of its stockholders are citizens of the State of New York.

(c) The Corollary of the proposition that the stockholders of the defendant corporation are citizens of New York.

It would involve a manifest absurdity to say, in the light of this presumption, that the complainants, who are stockholders and members of the Sol Sayles Company, are not citizens of the State of New York, when it is solemnly declared, that for the purpose of giving jurisdiction over the corporation, they are such citizens.

It is a physical impossibility that the complainants should be citizens of New Jersey and of New York at the same time, for the purpose of jurisdiction. If they are presumed as matter of law to be citizens of New York, in order to constitute the Sol Sayles Company, a citizen of that State, and such presumption overcomes the actual facts, then it seems impossible, that in the same breath they should be permitted to say that they

are citizens of New Jersey. And if they are citizens of New Jersey, then it would seem to be absurd to say that the corporation, jurisdiction of which depends upon the citizenship of its members, is a citizen of the State of New York, or of any State other than that of which its stockholders are citizens.

It may be urged that the presumption of the citizenship of the members of the corporation, which has been laid down in so many of the cases, is a legal fiction. But even though this be so, it seems impossible, that a legal fiction shall not be carried to its logical conclusion in the very proceeding in which such fiction is indulged. Would it not be the height of the ridiculous, to say, that, although by a legal fiction the defendant corporation is to be deemed a citizen of New York, because all of its stockholders are as a matter of law presumed to be citizens of that State, in the same breath to declare that, for the purpose of suing that corporation, of which they are members, they are citizens of another State? That would be blowing hot and cold with a vengeance, and would nullify what the authorities declare to be, a conclusive, indisputable, and irrefutable presumption, at the very instant when the presumption is indulged.

In effect the complainants come into court and say:

"We are stockholders of a corporation, every member of which is a citizen of New York, and, therefore, this court must consider the corporation a citizen of that State; but although as such stockholders we are citizens of New York, nevertheless, because we are in fact citizens of New Jersey, we ask the Federal Court to assume jurisdiction on the ground of a diversity of citizenship."

It would indeed be a singular species of legal legerdermain which would, in the same suit, uphold this legal fiction as to the citizenship of the defendants when considering the situs or so-called citizenship of the corporation, and then immediately declare that the fiction had ceased to exist when the Court came to inquire of what State the complainants were citizens.

Such a course would result in the nullification of what the courts declare to be an indisputable legal presumption, would be illogical and involve a judicial absurdity.

(*d*) *The Authorities cited for Appellants.*

The appellants, while recognizing the logic of this proposition, insist that the appellees are precluded from making the point now raised, by the decisions in

Dodge v. Woolsey, *18 How., 331.*
Hawes v. Oakland, *104 U. S., 450.*
Quincy v. Steel, *120 U. S., 241.*
Pollock v. Farmers' L. & T. Co., *157 U. S., 429.*
Cotting v. Kansas City Stock Yard Co., *183 U. S., 79.*

It is respectfully submitted that none of these cases will be found, on inspection, to militate, to the slightest extent, against the appellees' contention.

1. In *Dodge v. Woolsey* (*supra*) the Court undoubtedly assumed jurisdiction of a case, in which a corporation was sued by one of its stockholders, but the proposition here advanced by the defend-

ants was not presented or considered in any way. Moreover, the question involved in that case was, whether a tax, which had been imposed, was in violation of the United States Constitution, and as the existence of a Federal question will confer jurisdiction, irrespective of diversity of citizenship, the mere fact that the Court actually assumed jurisdiction, cannot be regarded as an authority against defendants' contention herein.

Moreover, that case was distinguished and limited in *Hawes v. Oakland* (*supra*).

It is further to be observed, that *Dodge v. Woolsey* arose prior to the Act of 1875, relating to the jurisdiction of the United States Circuit Court, and to the promulgation of the doctrine as to the alignment of parties, first suggested in the *Removal Cases*, *100 U. S.*, *457*, which will be more fully considered under the next point.

2. In *Cotting v. Kansas City Stock Yard Co.* (*supra*) jurisdiction of a litigation between stockholders of a corporation and the corporation, and others, was assumed by the Federal Courts, but the question involved, as in the preceding case, was a constitutional question, being, to use an expression made use of in the opinion at page 113, "simply a challenge to the constitutionality of a statute."

The proposition which counsel here presents does not appear to have been presented to the Court in that case and for the reason already stated, will have been futile.

3. In *Pollock v. Farmers' Loan and Trust Co.* (*supra*), a constitutional question was likewise presented, the constitutionality of the Income

Tax being the issue in the case, based entirely on a violation of the Federal Constitution and hence jurisdiction existed, independently of the citizenship of the parties.

In all of the above cases, constitutional questions were alone involved, and the citizenship of the respective parties did not, and could not, determine the right of jurisdiction exercised by the Federal Courts. Moreover, the question as to the conclusive presumption, that stockholders of a corporation must be deemed citizens of the State where the corporation was incorporated, was not presented in any way.

4. *Hawes v. Oakland (supra)*, which is also cited by the appellants, is not an authority on this proposition, because the question here involved was not considered or discussed; nor was jurisdiction entertained, the bill of complaint having been dismissed by the Circuit Court, and such dismissal having been approved by this Court.

Furthermore, that case pointed out, in most emphatic language, the abuses which had sprung up under the decision in Dodge v. Woolsey; and that those abuses have continued down to the present day, has nowhere been more emphatically expressed than in the opinion of the United States Circuit Court of Appeals, for the Second Circuit, in *De Neufville v. New York & Northern Railway Co., 81 Fed. Rep., 10, 13*, which is cited on the appellants' brief.

5. The case of *Quincy v. Steel (supra)* is likewise a case in which the Court refused to entertain jurisdiction, and hence cannot be authority for the appellants. The following significant language is

to be found in the opinion of Mr. Justice MILLER in that case:

"We are of opinion that the demurrer of the City of Quincy should have been sustained, for the reason that Mr. Steel shows no sufficient ground why he should have been permitted as a stockholder of the gas company to sustain this bill. In order to do this the circumstances must be such as to justify the Court, in the interest of justice, to override two cardinal principles of Federal jurisprudence. One of these is, that the litigants in the Federal Courts, where the right to sustain such litigation depends upon the citizenship of the parties, shall be citizens of different States. In this case the real right of action and the real contest before the Court, if it had proceeded, would have been between the two corporations, organized under the laws of Illinois, and existing and doing business in the same place, to wit, the gas company and the City of Quincy."

6. The appellants have also cited *Utah-Nevada Company v. De Lamar, 133 Fed. Rep., 113*, but it will be found that there, the case was remanded to the State Court, for lack of jurisdiction, and, although the question here involved was discussed, whatever the Court said upon that subject was clearly *obiter;* as was also the case in *Hanchett v. Blair, 100 Fed. Rep., 817*, which is cited as authority.

In both of those actions, the plaintiffs, although stockholders of the defendant corporations, were not suing in the right of the corporation to which they severally belonged.

In *Hanchett v. Blair*, the plaintiff sought to foreclose a mortgage which was given to him by the corporation. The decree rendered in the action

was one which was not in favor of the corporation, but against it. The recovery was in his favor, and for his sole benefit, and not in favor of, or for the benefit, or in the interest of the corporation.

In the *De Lamar Case* the plaintiff sued to recover a large sum of money owing by the corporation to the plaintiff's assignor under an agreement for the purchase of mining property. There, the recovery was likewise for the benefit of the plaintiff, and he was suing solely in his own right, and in no possible, or conceivable, sense for the benefit of the corporation, and that fact is emphasized in the opinion.

7. Finally, the appellants rest their argument upon the *94th Rule in Equity*, and argue that if the appellees' present contention were correct, that rule would not have been promulgated.

(*a*) That is not, however, a correct interpretation of the rule. It applies to all cases brought in the Federal Courts against a corporation; even to a case where a Federal question is involved, as, for example, such questions as came up in *Dodge v. Woolsey*, *Pollock v. Farmers' Loan & Trust Co.*, and *Cotting v. Kansas City Stock Yard Co.*

Even in such a case compliance with the rule must be shown. That is clearly indicated by a recent decision of this Court in *Davis & Farnum Mfg. Co. v. Los Angeles*, *189 U. S.*, *220*.

(*b*) Moreover, this rule would receive full effect in certain cases where there is a diversity of citizenship, where there has been an alignment of parties under the rule, which will be considered under the next Point. Thus, for instance, if suit were brought against the directors of a corpora-

tion, and other parties dealing with the corporation in fraud of the rights of stockholders, in the United States Circuit Court, in a district in which such defendants other than the corporation are defendants. In such a case, by arranging the parties according to their interests, there might be a diversity of citizenship, such as would confer jurisdiction upon the Federal Courts. In such a case it would be important, under Rule 94, to show that the suit is not a collusive one, as, for instance, that the complaining stockholders did not become such for the purpose of enabling them to bring a suit in the Federal Courts. Thus, for example, if this suit had been brought in Pennsylvania, and the Harringtons and Sayles, Zahn Company had been citizens of that State, and the complainants citizens of New Jersey, and the Sol Sayles Company a citizen of either New York or New Jersey, in such a case the Federal Courts, by aligning the Sol Sayles Company with the complainants, would doubtless take cognizance of the action, unless the fact were not negatived that the complainants had become stockholders for the collusive purpose of bringing this action.

(*c*) Furthermore, Rule 94 did not and could not enlarge the jurisdiction of the Federal Courts. The Courts of the United States have no jurisdiction, except such as is conferred upon them by the Federal Constitution and by the acts of Congress. They cannot create jurisdiction for themselves, and can exercise only such as has been expressly granted to them. They may establish rules of practice, but Rule 94, so far as it has any bearing upon the procedure in the Federal

Courts, is a rule of limitation rather than one of enlargement. Compliance with it may in some cases assist the Court in determining the proper attitude of the parties, with relation to their interests in the controversy, yet compliance with it is not conclusive, for the Court will determine the question of jurisdiction, and also the real status of the parties, as distinguished from their apparent status.

(*d*) Again, the enforcement of Rule 94 has had a tendency to restrict rather than to multiply the cases which have come into the Federal Courts, and it is, therefore, difficult to perceive how that rule can be considered as impeding the application of the Acts of Congress, which defines the jurisdiction of the Federal Courts, as they have been construed and applied in the numerous cases which we have cited. In other words, Rule 94 has no application to any cases, except those over which the Court has statutory jurisdiction.

II.

This suit being a derivative one, in which the complainants are suing solely for the benefit of the Sol Sayles Company, a New York corporation, that corporation, although in form a defendant, is, in legal effect, on the same side of the controversy as the complainants, and, since it is a citizen of the same State as the remaining defendants, the Federal Courts have no jurisdiction, as the suit does not involve a controversy between citizens of different States.

The nature of this suit has been fully considered under Point I. The authorities which are there cited, demonstrate the proposition, that the complainants cannot maintain this suit except in the right of the Sol Sayles Company, and that their right to relief must be tested by the right of the Sol Sayles Company to obtain redress for the alleged wrongs, which are set forth in the bill of complaint.

Shortly after the passage of the act of March 13, 1875, relating to the jurisdiction of the United States Circuit Court, the question arose as to whether the Federal Court was bound, as it apparently was under the previous legislation, to take or deny jurisdiction by the position which the

parties occupied in the pleadings, either as plaintiffs or defendants.

One of the first cases in which that question was presented was *Arapahoe County v. Kansas Pacific Railway Co., 4 Dillon, 277; s. c., 1 Fed. Cas., 1080,* decided by Mr. Justice MILLER, who was then a member of this Court. The action was brought by the plaintiff, a citizen of Colorado, who filed a stockholder's bill in the State Court of Colorado, making the Denver Pacific Railway Company, of which it was a stockholder, and which was incorporated under the laws of Colorado, and also its directors, as well as the Kansas Pacific Railway Company, a citizen of Kansas, defendants. The Kansas Pacific Railway Company and the individual defendants, applied to remove the suit to the Circuit Court of the United States, under the act of March 3, 1875, and it was held that the suit was removable, on the ground that the Denver Pacific Railway Company, although a defendant, was to be treated as a complainant. The following extended extract from the opinion is submitted as conclusive in support of this contention:

"The case then rests upon the question of whether the fact that the Denver Pacific Railway Company is a party defendant, and is a citizen of the same State of the party plaintiff, ousts the jurisdiction of this court or defeats the right of removal of the other parties who are citizens of other States. That question does not rest upon the same principle as the case of Messrs. Sayre and Moffat. The Denver Pacific Railway Company is a necessary party to this suit; it is one without which the suit cannot proceed. The main object of this suit, aside from obtaining a temporary injunction, and the appointment of a receiver, is to obtain an accounting with the Kansas Pacific

Railway Company and other defendants, on an allegation that a majority of the trustees of the Denver Pacific Railway Company have been committing frauds, and thus depriving that company of the funds belonging to it. The relief sought is an accounting, and the relief asked is a decree in favor of the Denver Pacific Railway Company for the amount found due upon that accounting. The Denver Pacific Railway Company is a necessary party to that accounting. A party cannot be required to go to all the trouble of accounting and having a decree, when that accounting and decree will not be a valid defense against the principal party having the right to call such party to account. If the suit was merely between the county commissioners and these trustees, the decree would not protect the trustees, whether they were decreed to pay over moneys, or whether they were discharged or acquitted. It would be no protection against the Denver Pacific Railway Company in another suit upon the same cause of action. This shows very clearly that the Denver Pacific Railway Company is not a mere nominal party, but is an indispensable party. But, as already stated, the main relief sought in this case will be, if the suit is successful, a decree in favor of the Denver Pacific Railway Company for the amount found due from the other defendants in this case. That is an important and significant feature of the transaction. In an action at law a suit could not be maintained in which the Board of Commissioners of Araphoe County should be plaintiffs, and the Denver Pacific Railway Company and these petitioners defendants, in which a judgment should be asked for One hundred thousand dollars in favor of the Denver Pacific Railway Company against itself and its co-defendants. The Court would say, you cannot make two defendants litigate before a jury and get a verdict as between themselves, while the party who brought the suit looks on as having no interest in the transactions. But the flexibility of the mode of proceedings in a Court

of Chancery is such that, for the attainment of justice, you may, in some instances, where the party is not before the Court, make him a defendant, when he will not be a plaintiff. You cannot compel him to hazard the results of a defeat, though his presence in the court may be necessary for the rights of somebody else, and his rights be with the plaintiff in the case. In suits at common law he would be there as plaintiff, if there at all. By the rules and practice in equity the court allows him to be defendant in the case; but the mere fact that he is placed as defendant instead of plaintiff in a suit in chancery, never changes his relation to the controversy in the case, and it is very clear that the interest of the Denver Pacific Railway Company is the interests of the plaintiffs; that their interest is identical—that the Board of County Commissioners are using the name of the Denver Pacific Railway Company to carry on this suit solely for the benefit of that company. The Denver Pacific Company, being in the control of the defendants, refused to bring this suit, and the complainants, stockholders of that company, were of necessity compelled to make it defendant, that it might be brought before the court; but when before the court, the company is entitled to recover against the other defendants. The complainants recognize this themselves, for in their prayer for relief they say expressly what they pray for is a decree in favor of the Denver Pacific Railway Company against the Kansas Pacific Railway Company and the other defendants. Now, the controversy in this case is one in which the Commissioners of Araphoe County and the Denver Pacific Railway Company are on one side, citizens of the State of Colorado, against all the other defendants. And all the other defendants are citizens of other States, except Sayre and Moffat, and the controversy, in the language of the constitution and of the statutes, is one between citizens of the State of Colorado and citizens of other States, and therefore within the meaning of the Constitution of the United

States, and within the meaning of the statute under which this removal is sought. The statute says, in the second section, 'that any suit of a civil nature, at law or equity, now pending or hereafter brought in any State court, where the matter in dispute exceeds, exclusive of costs, the sum or value of Five hundred dollars, and arising under the Constitution or laws of the United States, or treaties made, or which shall be made under their authority, or in which the United States shall be plaintiff or petitioner, or in which there shall be a controversy between citizens of different States, or a controversy between citizens of the same State, claiming lands under grants of different States, or a controversy between citizens of a State and foreign States, citizens or subjects either party may remove said suit into the Circuit Court of the United States for the proper district; and when, in any suit mentioned in this section, there shall be a controversy which is wholly between citizens of different States, and which can fully be determined as between them, then either one or more of the plaintiffs or defendants, actually interested in such controversy, may remove said suit to the Circuit Court of the United States for the proper district.'

"The best judgment that I am able to give is that this is a controversy between citizens of the State of Colorado on one side, and citizens of other States on the other side, and is properly subject to removal."

Citing this decision in *Walden v. Skinner, 101 U. S., 589*, Mr. Justice CLIFFORD referred to it as "decisive authority."

This doctrine was speedily adopted by this Court, and has been since applied in innumerable cases, a long line of which is cited on page 292 of Vol. 4 of Federal Statutes Annotated, title "Judiciary."

Special attention should be given to

The Removal Cases, 100 U. S., 457.
Pacific Railroad v. Ketchum, 101 U. S., 289.
Harter v. Kernochan, 103 U. S., 562.
Evers v. Watson, 156 U. S., 532.
Brown v. Truesdale, 138 U. S., 389, 395.
Merchants Cotton Press Co. v. N. A. Insurance Co., 151 U. S., 385.
Wilson v. Oswego Agency, 151 U. S., 63.

In *Harter v. Kernochan* (*supra*) the plaintiff, a township in Illinois, and a taxpayer thereof, on behalf of himself and other resident taxpayers, filed their bill in a court of that State against certain State, county and township officers, and the unknown owners and holders of certain township bonds, to restrain the levy and collection of a tax to pay the principal of the bonds or any interest thereon. A, a citizen of another State, was the owner of all of them. It was held that he was entitled to remove the suit to the Circuit Court of the United States, although the township officers were parties defendant with him. Mr. Justice HARLAN, however, said:

"We do not doubt that the suit was one which the defendant was entitled, under the act of March 3, 1875, c. 137, to remove from the State court. Disregarding, as we may do, the particular position whether as complainants or defendants, assigned to the parties by the draughtsman of the bill, it is apparent that the sole matter in dispute is the liability of the township upon the bonds; that upon one side of that dispute are all of the State, county, and township officers and taxpayers, who are made parties, while upon the other is Kernochan, the

owner of the bonds whose validity is questioned by this suit. He alone, of all the parties, is, in legal sense, interested in the enforcement of liability upon the township. It is, therefore, a suit in which there is a single controversy, embracing the whole suit, between citizens of different states, one side of which is represented alone by Kernochan, a citizen of Massachusetts, and the other by citizens of Illinois."

In *Covert vs. Waldron (33 Fed. Rep., 311, 312)* it was said:

"Where a Federal question is not involved, nor the conflicting grants of different States are in question, the controversies of which the Circuit Courts of the United States are given original cognizance must be between citizens of different States, or between citizens of a State and foreign citizens or subjects. It is abundantly settled by authority that, in arranging the parties relatively to the controversy between them, the mere form of the pleading may be set aside, and the parties placed on different sides of the matter in dispute, according to the facts. When, upon such an arrangement, it appears that citizens of the same state appear on both sides of the controversy, the controversy is not within the jurisdiction of the Circuit Court. Removal Cases, 100 U. S., 457; Railroad v. Ketcham, 101 U. S., 289; Barney v. Latham, 103 U. S., 205; Carson v. Hyatt, 118 U. S., 279; Blake v. McKim, 103 U. S., 336."

The same rule is laid down in other cases.

Cilly vs. Patton, 62 Fed. Rep., 498, 500.
Board of Trustees vs. Blair, 70 Fed. Rep., 414, 417.
Consolidated Water Co. vs. Babcock, 76 Fed. Rep., 642.

In *Shipp vs. Williams, 62 Fed. Rep., 4,* a bene-

ficiary under a deed of trust filed a bill against the debtor and the trustee to foreclose the deed of trust, the trustee having refused to act. The trustee and the debtor were citizens of the same State. It was held that the United States Circuit Court had no jurisdiction since the trustee, although a defendant, was really on the same side of the case as the beneficiary. Mr. Justice LURTON said:

"In courts of the United States, where the jurisdiction depends upon citizenship, all the co-plaintiffs must be competent to sue; and, if there is more than one defendant, each must be liable to be sued in those courts. If a trustee is, by his citizenship, qualified to sue in a Federal Court, the citizenship of the beneficiary under the trust is wholly unimportant. If the trustee is disqualified by reason of citizenship in the same State as that of the necessary defendants, the suit cannot be entertained, even though the beneficiary might be qualified. The jurisdiction is to be determined, in all such instances, by the citizenship of the trustee. Coal Co. v. Blatchford, 11 Wall 172. Neither is the rule changed by the refusal of the trustee to act. His refusal may authorize the beneficiary to exhibit a bill against the debtor to obtain a decree of foreclosure. But, if the legal title to the property conveyed in the trust be in the trustee, then the court could not grant any relief until the trustee was made a party defendant. * * * The duty of arranging parties according to their interests applies as well in cases of original jurisdiction under the first section of the act of March 3, 1875, as it does under the removal section of the same act. Arranging the parties to this suit according to their interests operates to place Woodworth and Wheeler on the same side of the case occupied by the complainants. We then have a case where some of the complainants are citizens of the same State as the defendants. Jurisdiction is thereby defeated."

To the same effect are

Gardner vs. Brown, 21 Wall., 36.
Pittsburg, C. & St. L. Ry. Co. vs. B. & O. R. R. Co., 61 Fed. Rep., 705.
Boston Safe Deposit & Trust Co. vs. City of Racine, 97 Fed. Rep., 817.
Old Colony Trust Co. vs. Atlanta Railway Co., 100 Fed. Rep., 798.
1 Foster's Federal Practice, p. 64.

As against these authorities, the appellants cite *Dodge v. Woolsey,* and the other authorities which have been reviewed under Point I.

Dodge v. Woolsey arose before the doctrine of the alignment of parties was suggested, and at a time when the Judiciary article relating to jurisdiction was couched in language which differed materially from the present act.

In the other cases cited, the question of the arrangement of parties was not suggested or considered, and the Court either dismissed the suits on sufficient grounds or had the right to entertain jurisdiction, not on the theory of diversity of citizenship, but because a Federal question was involved in the litigation.

Rule 94 is also cited in this aspect of the case, but what has been said with regard to that rule, under Point I., applies with full force here.

In the *De Neufville Case,* cited on pages 10, 11 of appellants' brief, it is very clear that the United States Circuit Court of Appeals, for the Second Circuit, felt that sound public policy required the application of the principle of arrangement of the parties, which the Court described as a "wholesome rule," but apparently felt precluded

from enforcing it by an erroneous and hasty reading of Rule 94, and of the decisions in *Hawes v. Oakland*, *Dodge v. Woolsey* and *Quincy v. Steel*, which, as we believe, we have fully explained.

Judge Lacombe, who united in that decision, and who rendered the decree now under review, has apparently revised his conclusions, and has applied the rule dictated by logical consistency, and sound public policy.

From a practical standpoint, it is believed, that the application of the principles for which we are contending, will do much to relieve the Federal Courts from a class of litigation, which naturally belongs in the State Courts, and which is sought to be taken out of the jurisdiction where it justly belongs by artifice, and, generally, from motives which will not bear close investigation.

In closing this brief, we wish to impress the point upon the Court, that there is no Federal question presented in this suit. The action is brought to set aside a judgment recovered in the Supreme Court of the State of New York against the Sol Sayles Company, by the Harringtons, and to compel the latter to restore to the treasury of the Sol Sayles Company, the specific property, which was sold by the Sheriff, under the execution issued on the judgment recovered in the State Court.

III.

The lack of jurisdiction of the Court can be raised at any stage of the litigation, and even though the appellees had not raised the question, the Court could, of its own motion, have dismissed the cause for want of jurisdiction.

The following cases abundantly support the above proposition, and appear to be conclusive on the question.

Grace v. American Cen. Ins. Co., 109 U. S., 278, 284.
Mexican Cen. R. R. Co. v. Pinkney, 149 U. S., 194.
Thomas v. Board of Trustees, 195 U. S., 207.

In *Grace v. American Cen. Ins. Co. (supra)*, at p. 283, it was said:

"The record in this case presents a question of jurisdiction which, although not raised by either party in the Court below, we do not feel at liberty to pass without notice. * * * As the jurisdiction of the Circuit Court is limited, in the sense that it had no other jurisdiction than that conferred by the Constitution and laws of the United States, the presumption is that a cause is without its jurisdiction, unless the contrary affirmatively appears."

As a result of its decision, the Court held that as the record did not affirmatively show the diverse citizenship of parties, the record did not "dis-

close a case of which the Court below could take cognizance."

In the *Mexican Cen. R. R. Co.* case (*supra*) the rule was thus stated, by Mr. Justice JACKSON, at p. 200:

"The proposition is not controverted that if it appears in the course of the trial that the controversy is not one of which the Court could take cognizance, by reason of the citizenship of the parties to it, the Circuit Court has the right, and it is its duty, to dismiss the cause for the want of jurisdiction."

The language of Mr. Justice HARLAN in *Thomas v. Board of Trustees* (*supra*) is likewise most significant:

"It is equally well established that when jurisdiction depends upon diverse citizenship the absence of sufficient averments or of facts in the records showing such required diversity of citizenship is fatal and cannot be overlooked by the Court, even if the parties fail to call attention to the defect or consent that it may be waived. Mansfield C. & L. M. Ry. Co. v. Swan, 111 U. S., 379; Martin v. B. & O. R. R Co., 151 U. S., 673, 689; Powers v. Chesapeake & Ohio Ry., 169 U. S., 92, 98. As late as in Minnesota v. Northern Securities Co., 194 U. S., 48, 62–63, we said, both parties insisting upon the jurisdiction of the Circuit Court: 'Consent of the parties can never confer jurisdiction upon a Federal Court. If the record does not affirmatively show jurisdiction in the Circuit, we must, upon our own motion, so declare and make such order as will prevent that Court from exercising an authority not conferred upon it by statute.' So that the fact stated in the certificate, that neither party in the Circuit Court objected to its jurisdiction is of no consequence."

IV.

It is respectfully submitted that the decree appealed from should be affirmed, with costs.

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